

Message Text

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TAGS: ECON, EFIN, NATO

SUBJECT: ECONADS: APPRECIATION OF ECONOMIC POSITION OF NATO
AND WARSAW PACT COUNTRIES FOR THE PERIOD THROUGH 1982

REF: A) STATE 238554; B) USNATO 6243; C) USNATO 6351;
D) USNATO 6408

1. AT ECONOMIC COMMITTEE MEETING NOVEMBER 21, CHAIRMAN
SUBMITTED REVISED APPRECIATION (AC/127-WP/407(2ND REVISE))
WHICH INCORPORATES ALL CHANGES SUGGESTED BY US (REFS A AND B).
ALTHOUGH NOT KNOWN TO OTHER DELEGATIONS, REVISED REPORT
ACTUALLY DRAFTED NOVEMBER 19 BY ECONOMIC DIRECTORATE AND
MISSION ECONOMIC COUNSELOR WORKING TOGETHER. QUOTED BELOW
(PARA 3) IS THE TEXT OF THE INTRODUCTION, THE SUMMARY
APPRAISAL WHICH IS DRAWN FROM RESOURCES PARAGRAPHS OF
MINISTERIAL GUIDANCE (REF C), AND PARAGRAPHS 23 AND 24
WHICH DEAL WITH KEY FACTORS OF ECONOMIC GROWTH OF NATO
MEMBERS THROUGH 1978 AND FROM 1978 TO 1982. REMAINDER OF
REPORT, TEXT OF WHICH IS TOO LENGTHY TO TRANSMIT BY CABLE,
SUPPORTS SUMMARY APPRAISAL WHICH, AS REQUESTED BY WASH-
INGTON, NO LONGER REFERS TO MORE FAVORABLE ECONOMIC GROWTH
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PROSPECTS FOR NORTH AMERICA AS COMPARED TO NATO EUROPE
AND DISTINGUISHES BETWEEN OUTLOOK FOR USSR AND OTHER WARSAW
PACT COUNTRIES. ECONADS WILL MEET AGAIN NOVEMBER 22 TO
REVIEW AND APPROVE REPORT WHICH IS NOW NEARLY TWO MONTHS

OVERDUE, FOR TRANSMITTAL TO DEFENSE REVIEW COMMITTEE (DRC).

2. ACTION REQUESTED. UNLESS INSTRUCTED OTHERWISE PRIOR TO ECONOMIC COMMITTEE MEETING MORNING OF NOVEMBER 22, MISSION WILL SUPPORT APPROVAL OF APPRAISAL.

3. QUOTE.

INTRODUCTION

THE FIRST ECONOMIC APPRECIATION (1) PREPARED IN 1972-73 COVERING THE PERIOD UP TO 1980, WHILE STILL VALID AS REGARDS THE EVALUATION OF THE MAIN ECONOMIC FACTORS INFLUENCING DEFENCE, WAS BASED ON THE ASSUMPTION THAT NO RADICAL CHANGES WOULD TAKE PLACE IN WORLD POLITICAL AND ECONOMIC RELATIONSHIPS. FOLLOWING THE STRONG WORLDWIDE INFLATIONARY DEVELOPMENT AND THE SERIOUS DETERIORATION OF THE BALANCE OF PAYMENTS OF MOST NATO COUNTRIES THE PERIOD UP TO 1982 HAS WORSENED DRASTICALLY. THE SAME SEEMS TRUE FOR MOST EAST EUROPEAN COUNTRIES. HOWEVER, FOR THE USSR THE ECONOMIC DEVELOPMENTS IN THE WEST HAVE, IF ANYTHING, MADE THE OUTLOOK SLIGHTLY MORE FAVOURABLE THAN THAT DESCRIBED IN THE PREVIOUS APPRECIATION.

2. THE LONGER TERM EFFECTS OF THE FUNDAMENTAL ECONOMIC CHANGES WHICH HAVE TAKEN PLACE SINCE 1973 ARE VERY DIFFICULT TO FORESEE AT THIS EARLY STAGE, PARTICULARLY FOR THE NATO MEMBER COUNTRIES, AND ONLY TENTATIVE FORECAST COULD BE MADE. THE FIRST PART OF THE APPRECIATION, WHICH COVERS ECONOMIC DEVELOPMENTS IN NATO COUNTRIES AND THE ECONOMIC BASIS FOR DEFENCE IN THESE COUNTRIES, HAVE BEEN BASED ON CERTAIN ASSUMPTIONS. IT HAS BEEN ASSUMED THAT THE CURRENT INFLATIONARY PROBLEM IS BROUGHT UNDER CONTROL, THAT THE RECYCLING OF THE OIL EXPORTING COUNTRIES' INCOMES IN THE INTERNATIONAL MONETARY SYSTEM IS SUCCESSFULLY ARRANGED AND THAT THE RESTRUCTURING AND READJUSTMENT PROCESSES DEVELOP SMOOTHLY IN WESTERN ECONOMIES.

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3. THE SECOND PART OF THE REPORT COVERS THE ECONOMIC DEVELOPMENT IN WARSAW PACT COUNTRIES AND THE DEVELOPMENT OF THE ABILITY OF THESE ECONOMIES TO SUPPORT THE DEFENCE EFFORT. THE EVALUATION OF THE PROSPECTS FOR THE WARSAW PACT COUNTRIES IN THE 1972-73 APPRECIATION REMAINS BROADLY VALID. THE IMPACT OF EXTERNAL DEVELOPMENTS ON THEIR ECONOMIES SHOULD BE FAIRLY LIMITED, ON THE WHOLE BENEFICIAL TO THE SOVIET UNION, DETRIMENTAL TO THE EAST EUROPEAN COUNTRIES

SUMMARY APPRAISAL

4. THE YEAR 1973 WAS A TURNING POINT FOR THE ECONOMIC DEVELOPMENT OF MEMBER COUNTRIES. UP TO THAT YEAR IT SEEMED

THAT THE GROWTH PERFORMANCE OF THE 1960S MIGHT BE REPEATED IN THE 1970S AND THAT THE STRENGTH OF THE ECONOMIES OF NATO COUNTRIES WOULD INCREASE SUBSTANTIALLY OVER THE PERIOD UNDER REVIEW, THUS PERMITTING A GREATLY IMPROVED RESOURCE BASE ON WHICH TO DRAW FOR DEFENCE PURPOSES. THE STRONG INFLATIONARY DEVELOPMENTS FROM 1972-73 AND THE FORESEEABLE BALANCE OF PAYMENTS PROBLEMS OF NATO COUNTRIES CREATED BY THE STEEPLY RISING ENERGY PRICES DURING THE LAST QUARTER OF 1973 HAVE COMPLETELY ALTERED THE GROWTH OUTLOOK FOR THE 1970S. THESE FACTORS AND INCREASINGLY DIFFICULT POLITICAL AND SOCIAL PROBLEMS HAVE MADE THE IMMEDIATE OUTLOOK VERY UNCERTAIN AND LED TO MORE FRAGILE ECONOMIC INTER-RELATIONSHIPS THAT MAKE LONG-TERM ECONOMIC PROJECTIONS HAZARDOUS. IN SUCH CIRCUMSTANCES THE POSSIBILITY OF RECESSION TAKING A GRIP CANNOT BE RULED OUT AND DECISIONS TAKEN BY ANY COUNTRY COULD HAVE CONSIDERABLE REPERCUSSIONS ON THE OTHERS.

5. EVEN SUPPOSING THAT NATO GOVERNMENTS CAN COPE WITH THE MANY DIFFICULT ECONOMIC PROBLEMS MENTIONED ABOVE, IN THE PRESENT FAR FROM CLEAR SITUATION, THE OUTLOOK POINTS TO REDUCED GROWTH RATES WITH INFLATION ONLY SLOWLY BEING BROUGHT UNDER CONTROL. UNDER THE BEST CONDITIONS IT WILL TAKE TIME FOR CORRECTIVE MEASURES TO TAKE EFFECT AND THEREFORE OVER THE PERIOD TO 1978 AVERAGE GROWTH RATES OF THE ORDER OF 2 PCT TO 3 PCT PER ANNUM APPEAR A REASONABLE PLANNING ASSUMPTION. GROWTH RATES MAY DIFFER FROM COUNTRY TO COUNTRY DEPENDING ON DEVELOPMENTS RELATING TO INFLATION,
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ENERGY SUPPLIES, THE BALANCE OF PAYMENT, THE LEVEL OF EMPLOYMENT AND THE CORRECTIVE POLICIES APPLIED. IF THESE POLICIES ARE SUCCESSFUL A GRADUAL IMPROVEMENT IN THE ANNUAL RATE OF GROWTH TO 3.5 PCT TO 4.5 PCT COULD BE EXPECTED AFTER 1978.

6. THE EVENTS THAT HAVE HIT NATO COUNTRIES ARE LIKELY TO HAVE AN OVERALL POSITIVE EFFECT ON THE SOVIET UNION SO FAR AS IT CAN TAKE ADVANTAGE OF HIGHER RAW MATERIAL PRICES IN EXPORT MARKETS, BUT POSSIBLE LESS FAVOURABLE OR EVEN ADVERSE EFFECTS ON OTHER WARSAW PACT COUNTRIES. NEVERTHELESS, EVEN THE LATTER WILL BE LESS AFFECTED THAN THE ALLIED COUNTRIES. ECONOMIC GROWTH COULD AVERAGE SOME 5 PCT PER YEAR IN THE SOVIET UNION AND INCREASE THE ECONOMIC STRENGTH OF THE WARSAW PACT.

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7. THE CONCENTRATION ON ARMAMENTS PRODUCTION IN THE USSR AND THE VERY CONSIDERABLE R & D EFFORT MADE OVER THE LAST DECADE PLACE THE USSR IN A RELATIVELY VERY FAVOURABLE POSITION TO MAKE OPTIMAL USE OF RESOURCES FOR MILITARY PURPOSES OVER THE COMING YEARS. THE RATE OF INCREASE OF MILITARY EXPENDITURES OF THE SOVIET UNION IS EXPECTED TO ACCELERATE TO 3 TO 5 PCT ANNUALLY FOR THE NEXT YEAR OR TWO AS CONVENTIONAL WEAPONS ARE REPLACED OR MODERNISED AND A NEW GENERATION OF STRATEGIC ARMS ARE BROUGHT INTO SERVICE. THIS REFLECTS A CYCLICAL DEVELOPMENT THAT IS EXPECTED TO LEAVE THE LONGER-TERM TREND IN MILITARY SPENDING IN THE SOVIET UNION AT A RATE OF THE ORDER OF 3 PCT YEARLY IN REAL TERMS.

8. WHILE, DUE TO THE ENHANCED ECONOMIC CAPABILITY OF THE SOVIET UNION, THE MILITARY POTENTIAL OF THE WARSAW PACT IS LIKELY TO INCREASE RELATIVELY RAPIDLY OVER THE PERIOD UNDER REVIEW, THE RESOURCES AVAILABLE TO DEFENCE IN MOST NATO COUNTRIES COULD INCREASE ONLY SLOWLY. IN BOTH THE EASTERN AND WESTERN GROUP OF COUNTRIES THE IMPACT OF ECONOMIC DEVELOPMENTS WILL VARY CONSIDERABLY. FOR NATO MEMBER COUNTRIES IN PARTICULAR, CIRCUMSTANCES ARE LIKELY TO ARISE THAT WOULD SERIOUSLY WEAKEN SOME ECONOMIES, AT LEAST
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IN THE MEDIUM-TERM. FOR THE HARDEST HIT COUNTRIES IMPLEMENTATION OF THE DEFENCE EFFORT HAS INDICATED IN THE 1975-1980 FORCE GOALS MIGHT BE DIFFICULT BECAUSE OF ECONOMIC AND POLITICAL PROBLEMS. THIS UNDERLINES THE NECESSITY OF OBTAINING THE MAXIMUM EFFECTIVE VALUE FROM THE RESOURCES THAT COUNTRIES ALLOCATE TO DEFENCE THROUGH RATIONALISATION AND CO-OPERATION IN ARMS PROCUREMENT ON A NATO-WIDE BASIS.

23. IN THE CURRENT CONFUSED INTERNATIONAL ECONOMIC SITUATION IT IS VERY DIFFICULT TO MAKE EVEN APPROXIMATE FORECASTS OF FUTURE ECONOMIC GROWTH. RECENT EEC AND OECD STUDIES VARY WIDELY IN THEIR ESTIMATES EVEN FOR THE YEAR 1975. FOR EXAMPLE, FOR THE FOUR MAJOR EUROPEAN COUNTRIES THE OECD, WITHOUT EXCEPTION, TAKES A CONSIDERABLY LESS OPTIMISTIC VIEW AND INDICATES A GROWTH RATE FOR THE COUNTRIES TAKEN TOGETHER, OF JUST OVER 1 PCT COMPARED WITH OVER 3 PCT IN THE EEC ESTIMATE. SUCH DIFFERENCES, ARE DUE TO THE ASSUMPTIONS ON WHICH THE PROJECTIONS ARE BASED. EVEN SUPPOSING THAT NATO GOVERNMENTS CAN COPE WITH THE MANY DIFFERENCES, ARE DUE TO THE DIFFICULT ECONOMIC PROBLEMS MENTIONED ABOVE, IN THE PRESENT FAR FROM CLEAR SITUATION, THE OUTLOOK POINTS TO REDUCED GROWTH RATES WITH INFLATION ONLY SLOWLY BEING BROUGHT UNDER CONTROL. UNDER THE BEST CONDITIONS IT WILL TAKE TIME FOR CORRECTIVE MEASURES TO TAKE EFFECT AND THEREFORE OVER THE PERIOD TO 1978 AVERAGE GROWTH RATES OF THE ORDER OF 2 PCT TO 3 PCT PER ANNUM APPEAR A REASONABLE PLANNING ASSUMPTION. GROWTH RATES MAY DIFFER FROM COUNTRY TO COUNTRY DEPENDING ON DEVELOPEMNTS RELATING TO INFLATION, ENERGY SUPPLIES, THE BALANCE OF PAYMENTS, THE LEVEL OF EMPLOYMENT AND THE CORRECTIVE POLICIES APPLIED.

(C) THE LONGER-TERM ECONOMIC OUTLOOK, 1978-1982

24. A GENERAL IMPROVEMENT IN THE ECONOMIC CONDITIONS OF MEMBER COUNTRIES MIGHT BE EXPECTED IN THE YEARS 1978 TO 1982. NATIONAL EFFORTS TO SAVE ENERGY AND TO INCREASE DOMESTIC PRODUCTION MUST BE EXPECTED TO HAVE MADE IMPORTANAT PROGRESS BY 1978. DURING THE FIVE YEAR PERIOD THROUGH 1982 FURTHER CONSIDERABLE IMPROVEMENTS MIGHT BE EXPECTED. SUCH A DEVELOPMENT WOULD PROGRESSIVELY ALLOW COUNTRIES TO DIRECT ECONOMIC RESOURCES FROM RESTRUCTURING PURPOSES ECONOMIC GROWTH POSSIBLE DURING THE LAST YEARS OF THE PERIOD. IF
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SUCCESSFUL, MEMBERS OF THE ALLIANCE COULD EXPECT A GRADUAL IMPROVEMENT IN THE ANNUAL GROWTH RATE TO 3.5 TO 4.5 PCT AFTER 1978.

(1) AC/127-D/436, 12TH APRIL, 1973

UNQUOTE.

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